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In the Supreme Court of the United States

OCTOBER TERM 1963

No. 968

UNION OIL COMPANY OF CALIFORNIA,
Appellant.

vs.

STATE BOARD OF EQUALIZATION OF THE STATE OF CALIFORNIA,
Appellee.

Appeal from the Supreme Court of the State of California

Jurisdictional Statement

HART H. SPIEGEL,
111 Sutter Street
San Francisco 4, California
Attorney for Appellant.

DUNCAN E. HAYNES,
111 Sutter Street
San Francisco 4, California

BROBECK, PHLEGER & HARRISON,
111 Sutter Street
San Francisco 4, California
Of Counsel.

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In the Supreme Court of the United States

OCTOBER TERM 1963

No.

UNION OIL COMPANY OF CALIFORNIA,
Appellant,

vs.

STATE BOARD OF EQUALIZATION OF THE STATE OF CALIFORNIA,
Appellee.

Appeal from the Supreme Court of the State of California

Jurisdictional Statement

Appellant appeals from the judgment of the Supreme Court of the State of California entered on November 14, 1963 affirming the judgment of the Superior Court of the State of California in and for the County of Sacramento and submits this Statement to show that the Supreme Court of the United States has jurisdiction of the appeal and that a substantial question is presented.

OPINION BELOW

The opinion of the Supreme Court of the State of California is officially reported at 60 A.C. 399 and unofficially reported at 386 P. 2d 496 and 34 Cal. Rptr. 872; the opinion of the District Court of Appeal is not officially reported but is unofficially reported at 28 Cal. Rptr. 58; the opinion of the Superior Court is not reported. Copies of the three opinions and the findings of fact and conclusions of law and the judgment are attached hereto as Appendix A.

JURISDICTION

The action is one for the recovery of use taxes collected by the State of California under the California Use Tax Law. Recovery of the tax is sought on the ground that the Use Tax Law is unconstitutional as applied in that it violates the due process clause of Amendment XIV to the United States Constitution. The action was brought in the state court pursuant to Cal. Rev. & Tax Code, Sec. 6933, Cal. Stats. 1957, ch. 807, sec. 6, p. 2021. The judgment of the Supreme Court of California was entered on November 14, 1963 and notice of appeal was filed in that Court on February 4, 1964. The jurisdiction of the Supreme Court to review this decision by direct appeal is conferred by Title 28, United States Code—Section 1257 (2), 62 Stat. 929 since there is drawn in question the validity of a statute of a state on the ground of its being repugnant to the Constitution of the United States, and the decision is in favor of its validity. The following decisions sustain the jurisdiction of the Supreme Court to review the judgment on direct appeal in this case: *Marcus v. Search Warrant*, 367 U.S. 717, 721 (1961); *Dahnke-Walker Co. v. Bondurant*, 257 U.S. 282 (1921). The statutes involved are Cal. Stats. 1941, ch. 36, sec. 1, pp. 533, 538 and Cal. Stats. 1948, ch. 12, sec. 4, p. 16. The texts thereof are set forth in Appendix B hereto.

QUESTION PRESENTED

This case involves the application of state use taxes to a new "billion dollar industry"—the equipment rental business. Leased equipment such as railroad rolling stock, trucks and trailers, construction equipment, ships and the like is taken by lessees into every state in the union. The California Supreme Court has held in the case at bar, that if a foreign corporation purchases movable equipment *outside* of California and leases it to a company which brings it *into* California and there uses it, the foreign corporation is "using" the equipment *in* California within the meaning of the California Use Tax Law and is therefore liable for a California use tax. In short, the California Supreme Court holds that use tax liability of the rental agency (the owner of the equipment) arises, *not in the state where the rental agency carries on its business of renting out the equipment, but in the state where the lessee drives the car or uses the equipment or operates the ship.* The use tax on the owner-lessor depends not on where he conducts *his* business, but on where the lessees conduct *theirs*.

As a step in reaching this result, the Court held that a foreign corporation which purchases property and delivers it outside the state to a lessee can be held *personally liable* for use tax by the state into which the lessee brings the property. Accordingly, this appeal presents the question: If a California statute *imposing personal liability* for use tax is interpreted so as to apply to a foreign corporation whose *only contact* with California is the ownership of property operated by its lessee in California, is it constitutional under the due process clause of the 14th Amendment to the United States Constitution?

STATEMENT OF THE CASE

Appellant, Union Oil Company of California, is a California corporation engaged in refining and transporting petroleum products in California and admittedly is subject to both the legislative and judicial jurisdiction of the State of California. Cienega Tanker Corp. ("Cienega") is a Delaware corporation whose sole contact with the State of California is that set forth below.[1]

In March of 1953, appellant sold and delivered two oil tankers to Cienega *in Oregon*. Immediately thereafter, Cienega leased the vessels (by bareboat charter) back to appellant for periods of 24 months and 48 months respectively and redelivered them to appellant *in Oregon*. Charter hire was to be paid and was paid in *New York*.

Following the sale, appellant, as lessee of the ships, operated them part of the time in California. The California Board of Equalization (Appellee) determined that Cienega, *the out-of-state owner and lessor*, incurred a use tax liability to California. It acknowledged that Cienega had purchased the vessels *outside* California but contended that it had used them *in* California on the theory that a lessor of property whose lessee brings the property into California is "using" the property in California. The Board also determined that appellant, which does business in California, as the vendor of the ships was required to collect the tax from Cienega. Appellant paid the tax and brought this suit for refund.[2]

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1. It is stipulated that Cienega does not do, and never has done, business in California; and does not have, and never has had any officers, agents or representatives to act for it in California. It is a non-resident corporation with no contacts or "presence" in California at all. Moreover, it is wholly unrelated—by stock ownership, directors, officers, employees or otherwise—to appellant.

2. As will be seen hereafter, Appellant, a California retailer who sold the property to Cienega, the foreign corporation, was re-

HOW THE FEDERAL QUESTION IS PRESENTED

In the Superior Court (the court of first instance) appellant argued in its opening brief:

> "We submit that settled constitutional principles of due process of law based on the Fourteenth Amendment to the Federal Constitution . . . preclude the instant tax.
>
> * * * * * * *
>
> "The 'link' between Cienega and the State of California . . . is . . . wholly lacking . . . in the present case."

The same argument was made in substance in appellant's reply brief in the Superior Court.

The Superior Court passed on this federal question as follows:

> ". . . But I must be consistent and . . . I must, and do, conclude . . . that jurisdiction to tax Cienega exists."

The constitutional question was raised in the intermediate appellate court (the District Court of Appeal) by arguing its applicability in the opening and reply briefs on file therein.[3] The District Court of Appeal did not rule on the federal question, however, for it reversed the trial court and ruled that the out-of-state owner and lessor was not using the property in California merely because its lessee used the property in the State. It was not therefore compelled to deal with the constitutional question.

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quired as a statutory tax collector to pay the tax to the state. The power of the state to make Union collect the tax if one is, in fact, due is not questioned; the question relates solely to the power of the state to create a liability for the tax in Cienega, the foreign corporation.

3. In appellant's opening brief, for example, it was argued that "the due process clause of the Fourteenth Amendment of the United States Constitution" barred imposition of the tax. (App. Op. Br. p. 19). The argument was reiterated in the reply brief (App. Reply Br. pp. 31-45).

The constitutional question was raised in the California Supreme Court in the answer to a Petition for Hearing. The Supreme Court considered the federal question and ruled that the statute was constitutional as applied in the following manner:

> "The due process clause requires 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.' . . . the instant situation displays 'the link': the use of the vessels impinged in California; California granted to them the benefits of an ordered society.
>
> * * * * * * *
>
> ". . . we see no constitutional violations in California's imposition of its use tax in this instance." (App. A. pp. 17-18)

All the requirements of Section 1257(2) of Title 28 of the United States Code, 62 Stat. 929 have therefore been met. Appellant from its first to its last briefs filed in the courts below argued consistently that the Use Tax Law as applied in this case violated the due process clause of the Fourteenth Amendment to the United States Constitution. The trial court and the Supreme Court considered the federal question on its merits and held the statute not repugnant to the United States Constitution as applied. This was a final judgment rendered by the highest court of the State of California in which a decision could be had. The jurisdiction of this Court on appeal is therefore clear. *Marcus v. Search Warrant*, 367 U.S. 717, 721 (1961); *Dahnke-Walker Co. v. Bondurant*, 257 U.S. 282 (1921).

THE QUESTION IS SUBSTANTIAL

As the California Supreme Court pointed out, the equipment leasing business has now "expanded to the magnitude of a billion dollar industry." See App. A. p. 8, fn. 5. Leased equipment enters every state in the Union. This

case has a critical bearing on how the use tax—a common state tax[4]—shall be applied to that industry. But it has even broader significance in terms of its far reaching consequences on state power to subject non-residents to *in personam* liabilities. The California Supreme Court holds that use tax liability on a rental agency (the owner of the equipment) is to be imposed by the state into which its lessee takes the equipment—not in the state where the rental agency carries on its own activities. This upside-down result will, if allowed to stand, create havoc in the industry. Every state where leased equipment is used by the lessee can be expected to take advantage of the way pointed by the California use tax authorities.

Not only is the owner-lessor faced with the intolerable administrative burden of determining into what states mobile equipment may have gone,[5] but according to the California Supreme Court, he is *personally liable* for use taxes levied by states with which he has no connection whatsoever, apart from the fact that property which he has leased out is brought into the taxing state by the lessee.

The California Supreme Court has simply and unequivocally held that the mere ownership of property in California is sufficient to empower California—not just to assess a tax on the property itself, for this power is admitted—but rather to make the owner of the property personally liable for the tax. The consequences of this decision are far-reaching. States may now subject foreign corporations (and presumably other non-residents) to *in personam* liabilities

4. 35 states now impose the tax. P-H All States Tax Guide, State and Local Tax Service, Page 104.

5. The ordinary equipment lease gives the lessor no right to receive reports on where the equipment is. In the instant case, the lessee was privileged to use the vessel "in any trade throughout the world" and was not required to and did not in fact keep appellant apprised of the vessel's location.

despite the fact that the sole nexus, link or connection between these foreign corporations and the state is the mere ownership of property located in the state.

It is respectfully submitted that this result extends the power of a state beyond the limits heretofore sanctioned by this Court and is founded upon a misinterpretation of fundamental principles of law.

There are two wholly distinct methods by which a state may acquire jurisdiction: jurisdiction may be founded *in rem* and jurisdiction may be founded *in personam*. Accordingly, while the ownership of property within a state will subject the owner to the state's *in rem* jurisdiction over the property, it is not, in and of itself, sufficient to subject the owner to the state's *in personam* jurisdiction.

Equally fundamental is the principle that ". . . jurisdiction is as necessary to valid *legislative* as to valid judicial action . . ." *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 342 (1954) quoting from *St. Louis v. Ferry Co.*, 11 Wall. 423, 430 (1870). Accord, *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 464-5 (1959); *International Shoe Co. v. Washington*, 326 U.S., 310, 321 (1945); *Connecticut General Life Ins. Co. v. Johnson*, 303 U.S. 77, 80 (1938).

Application of these two principles demonstrates that the location of property in a state confers *in rem* and *quasi in rem* jurisdiction in both the judicial and legislative arms of the state, thus enabling the state to impose a tax on property or transactions in the state (See e.g. *Coe v. Errol*, 116 U.S. 517 (1886); *Pullman's Palace Car Co. v. Pennsylvania*, 141 U.S. 118 (1891); and *New York ex. rel Whitney v. Graves*, 299 U.S. 366, 369 (1937) and enforce the payment of the tax by resort to its *in rem* jurisdiction (See e.g. *Shaffer v. Carter*, 252 U.S. 37 (1920) and cases cited below).

It is equally clear however that the location of the property in the state does not empower either the legislative or judicial arm of the state to go beyond the property and create a personal liability in its owner. Accordingly, as summarized neatly by Professor Beale,

> ". . . a tax may . . . be laid on land or a chattel within the territory, and its payment may be enforced *in rem*, but the tax cannot be made a personal obligation of the owner, upon whom the state has no jurisdiction to impose an obligation."

1 Beale, Conflict of Laws Section 118 B 5. Citing *Dewey v. Des Moines*, 173 U.S. 193 (1899); *New York v. McLean*, 170 N.Y. 374, 63 N.E. 380 (1902).[6]

A recent holding of this Court provides a reaffirmation of the principle described by Professor Beale. In *Miller Bros. Co. v. Maryland*, *supra*, it was recognized by this court that the Maryland judiciary had *quasi in rem* jurisdiction over the taxpayer due to the seizure by the state of the taxpayer's truck while located within the state. Moreover, the location of the truck in the state from time to time established that an apportioned *property* tax on this truck would have been upheld. *Pullman's Palace Car Co. v. Pennsylvania*, *supra*. Nevertheless, this court held that despite the presence of *quasi in rem* jurisdiction by the judiciary and *in rem* jurisdiction by the legislature, the legislature lacked *in personam* jurisdiction over the taxpayer.

In the instant case, both the trial court and the California Supreme Court conceded that some definite link, between a state and the person it seeks to tax, was needed to support

6. For the proper procedure of enforcing the tax in the manner described by Professor Beale see: *Nickey v. Mississippi*, 292 U.S. 393 (1934); *Shaffer v. Carter*, 252 U.S. 37 (1920) and *Bristol v. Washington County*, 177 U.S. 133 (1900) discussed cryptically by Professor Thomas Read Powell in Sales and Use Taxes—Collection From Absentee Vendors, 57 Harv. L. Rev. 1086, 1087, N. 7 (1944).

the tax; but both courts concluded that the "link" existed. The trial court sought to establish this "link" by stating that Cienega (the out-of-state owner-lessor) was "both using and consuming its property in California." App. A, p. 44. But clearly this is merely the affixation of a label to a set of facts, i.e., Cienega was an owner which had transferred possession of the property outside California to its lessee. In this context, the statement that Cienega "used and consumed" the property in California means only that Cienega *owned* property which its lessee had brought into California. In terms of "nexus" the trial court simply held that the ownership of leased property constituted a "use" of the property within the meaning of the California tax statutes, and this "use" provided the required link. But this bootstrap affiliation of the state with the taxpayer cannot be sustained. Surely a state cannot obtain jurisdiction over a taxpayer with which it has insufficient nexus (and the mere ownership of property is such an insufficient nexus as the very distinction between *in rem* and *in personam* jurisdiction demonstrates) simply by bestowing a title such as "use" on this insufficient nexus.

The California Supreme Court was equally gingerly when it faced the due process question. It attempted to dispose of the problem with the remark that:

> "The instant situation displays 'the link': the use of the vessels impinged in California; California granted to them the benefits of an ordered society." (App. A, pp. 17-18).

But to say that the owner's use of the vessels "impinged" in California, is unilluminating for the problem to decide is whether the "use" to which the court has reference provides sufficient nexus; and in this context, "use" as we have seen means merely the ownership of property by a non-resident

corporation. In terms of fact, place and circumstances, all the court has said is that a lessee brought the leased property into California—a fact which clearly does not give California jurisdiction to impose *in personam* liability on the out-of-state owner. Use of an ambiguous word such as "impinged" reflects the court's uncertainty in the matter. And the court's apparent reliance on the fact that California granted to the *vessels* "the benefits of an ordered society" highlights the manner in which *in rem* jurisdiction has been used as a fulcrum for imposing *in personam* liability.[7]

The California Supreme Court also cites *Cox v. Errol*, 116 U.S. 517 (1886), *Pullman's Palace Car Co. v. Pennsylvania*, 141 U.S. 18 (1891) and *New York ex. rel. Whitney v. Graves*, 299 U.S. 366 (1937). But these cases go only to the power to lay a tax on the property or to tax the income arising from a sale of property in the state (points not in issue here) and do not pertain to the power to create an *in personam* liability for the tax.

The California Supreme Court cites *Stone v. Stapling Machine Co.*, 220 Miss. 470, 71 So. 2d 205, appeal dismissed, 348 U.S. 802, rehearing denied, 348 U.S. 884 (1954) as passing "upon this exact issue." But in doing so the court fails

7. The violation of due process inherent in the State's position in this case is camouflaged by the fact that the State clearly does have jurisdiction over the tax *collector*, appellant (Union Oil Company). It has therefore had no difficulty in extracting the tax. *But the issue is not whether the State has jurisdiction to make a tax collector out of Union but whether it has jurisdiction to make a taxpayer out of Cienega.* The constitutional problem would be exactly the same and perhaps presented in more stark terms if Cienega had purchased the two oil tankers from an Oregon corporation having no connection with California and had then immediately leased the vessels to Union. Under these circumstances, California could not seize upon Union to make it a tax collector since it would not be the retail seller of the vessels; nor could it seize on the Oregon seller to make it a tax collector since the Oregon seller has no place of business in California. *Miller Bros. v. Maryland, supra.*

to note two facts. First, the taxpayer in *Stone* did not even raise the personal liability question until the last page of a Petition for Rehearing filed with this Court! Needless to say, the question was not timely raised and can hardly have been said to have been passed on by a dismissal of the appeal. See *Hanson v. Denckla*, 357 U.S. 235, 243-4 (1958). Second, the taxpayer's income in *Stone* bore a direct relationship to, and was dependent upon, the activity of the licensee in the state, 71 So. 2d at 207. In fact, the taxpayer admitted it was "doing business" in Mississippi and rested its defense on the ground that its business was solely interstate business to which a privilege tax could not apply. Appellant's Reply Brief, p. 12. Thus, the personal liability question which is present here was neither available nor raised in the *Stone* case.

Finally, the California Supreme Court seeks to distinguish the *Miller Bros. Co.* case from the instant case by relying on *Scripto, Inc. v. Carson*, 362 U.S. 207 (1959). But *Scripto* in no way detracts from the principles discussed herein for the court in *Scripto* simply held that the solicitation present in that case was sufficient to sustain *in personam* jurisdiction. There is no suggestion that those facts are paralleled in the instant case.

THE CONFLICT BETWEEN THE CALIFORNIA SUPREME COURT AND THE MAINE SUPREME COURT

The decision in the instant case is conceded to be directly contrary to two decisions of the Supreme Court of the State of Maine: *Trimount Coin Machine Co. v. Johnson*, 152 Me. 109, 124 A. 2d 753 (1956); *South Shoe Machine Co., Inc. v. Johnson*, 159 Me. 74, 188 A. 2d 353 (1963). In both of these cases the Maine Supreme Court held that the nonresident lessor was not liable for use tax to the State of Maine merely because its lessee brought the property into the State and

there used it.[8] The decisions of the Supreme Court of Maine are not only sound in their interpretation of the use tax law, but they avoid the constitutional difficulties which inhere in the California Supreme Court's decision in the instant case. In upholding personal liability for use tax on the out-of-state owner-lessor, who has no contact with the taxing state other than the ownership of property brought into such state by the lessee, the California Supreme Court permits imposition of the use tax in clear violation of the due process clause of the Fourteenth Amendment to the United States Constitution.

CONCLUSION

In this case the California Supreme Court holds that the out-of-state owner-lessor may be subjected to personal liability for California use tax despite the fact that such taxpayer does not do, and never has done, business in California; and does not have, and never has had, any officers, agents or representatives to act for it in California; and, in fact, has no "nexus" or "presence" in California whatsoever other than the fact that property which it owns was used by its lessee during a portion of the term of the lease in California. The extension of personal liability to an out-of-state entity under these circumstances is a clear denial of due

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8 The Maine Supreme Court's decision in Automatic Canteen Co. of America v. Johnson, 159 Me. 189, 190 A.2d 734 (1963) where it was held that an out-of-state lessor was subject to use tax was based solely on the fact that the out-of-state lessor had agents within Maine who exercised rights and powers over the property in Maine and therefore used it in the State. The Maine Supreme Court was careful to distinguish and approve of its prior decisions, which are analogous to the instant case, where the out-of-state lessor had no agents, representatives or other activities within the State to form the basis for imposition of a use tax.

process of law.[9] The far reaching effect of the decision in terms of extension of state power to subject foreign corporations to *in personam* liabilities warrants review by this Court.

Respectfully submitted,

HART H. SPIEGEL
Counsel for Appellant.

DUNCAN E. HAINES,
111 Sutter Street
San Francisco 4, California

BROBECK, PHLEGER & HARRISON,
111 Sutter Street
San Francisco 4, California
of Counsel

9. It is clear beyond question that California would not have *in personam judicial* jurisdiction over the non-resident Cienega. Yet in this case the California Supreme Court finds that California has *in personam legislative* jurisdiction. The anomaly is compounded by the fact that it has generally been thought the contacts or nexus needed to obtain legislative jurisdiction were more substantial than those for judicial jurisdiction. See generally, *Elcanon Isaacs, An Analysis of Doing Business*, 25 Colum. L. Rev. 1018, 1024 (1925); cf. *Ehrenzweig, Conflict of Laws*, Part One, Section 33 at 112, n. 20 (1959).

(Appendices follow)

Appendix A

In the Supreme Court of the State of California
In Bank

Union Oil Company of California,
Plaintiff and Appellant,
vs.
State Board of Equalization,
Defendant and Respondent.

Filed Nov. 14, 1963

OPINION

In this controversy as to the application of the California use tax to an extra-state sale and leaseback of two tankers we hold that an owner of property "uses" it under the tax statute when he leases it. The use of the lessor through the lease in California is a California use. The trial court's finding that the purchaser at the date of the transaction anticipated that the lessee would use the vessels in California, and the subsequent actual use in California, render the transaction a purchase for use in this state. Hence the purchaser is liable for the tax upon the basis of the purchase price. No constitutional prohibitions prevent California's application of its use tax to the transaction. We shall proceed, *infra*, to point out in more detail the reasons for these conclusions.

The case involves the attempt of Union Oil Company (hereinafter called Union) to recover the amount of $151,800 which Union, as tax collector, paid as use taxes for Cienega Tanker Corporation (hereinafter called Cienega), the true taxpayer.

The Board of Equalization assessed the tax in the view of the following facts. Union entered into a contract in

New Jersey to sell to Cienega the two bulk oil tankers, which, according to the contract, would immediately be leased back to Union. Union subsequently operated the tankers in California. Since the sale of the tankers occurred outside of California the sales tax did not apply. California, however, called upon Union to collect a use tax from Cienega. Sections 6203 and 6204 of the Revenue and Taxation Code require a retailer maintaining a place of business in this state to collect such a use tax. Union does not dispute that it is a retailer maintaining a place of business in this state. It maintains, however, that Cienega did not incur such a use tax liability, and that Union, as tax collector, should accordingly be refunded the amount of the tax.

The trial court found that the two vessels, the S.S. Santa Paula and S.S. Lompoc, "were purchased by Cienega from a retailer (Union) for use and consumption in the State of California and were used and consumed by Cienega in the State of California." The court therefore sustained the assessment. The finding rested upon the parties' stipulation of facts which discloses the details of the transaction.

Thus the parties entered into a contract at Jersey City, New Jersey, which provided that Cienega take legal title to the vessels and that physical possession be transferred at Astoria, Oregon or such other United States port as Union might designate. The purchase price for each vessel was $2,200,000. The contract further stipulated that concurrently with the delivery of the vessels Cienega would execute a bareboat charter for each vessel.[1] The period for

1. The terms of the charters reserve to Cienega certain rights incident to its ownership: a prohibition against illegal operation or the carrying of cargo that might expose either vessel to "penalty, forfeiture or capture," and another provision which imposes upon Union the obligation to drydock the vessels at least once annually and comply with a maintenance standard entitling the vessels "to the highest classification and rating of the American Bureau of

the charter for the S.S. Santa Paula was two years; that for the S.S. Lompoc, four years. Union enjoyed an option to extend the charter period for each vessel for one year.

The parties promptly executed the contract: Union delivered the ships to Cienega at Astoria, Oregon; Cienega concomitantly executed a bareboat charter for each vessel and redelivered physical possession to Union.

While we cannot assume that the sale and leaseback transactions were not bona fide, we note that the physical utilization of the two ships in the year immediately preceding, and the year immediately following, the transactions remained significantly consistent. Union did not deviate from the customary pattern of employment of the vessels. In the year preceding their transfers the Santa Paula and the Lompoc spent 252 and 289 days respectively in intrastate commerce in this state; in the year following the transfers these vessels spent 312 and 335 days respectively in predominantly California activity.

The parties do not dispute the fact that if any of the significant elements of the foregoing transactions had transpired within California the transfer would have been subject to our sales tax; since, however, no transfer of title or possession occurred in this state, no sales tax accrued. At the time of these events, moreover, neither the place of execution of the contract of sale (New Jersey) nor the point of delivery and redelivery of the vessels (Oregon) imposed either a sales tax or a use tax.

Shipping." In accord with these protective clauses, Cienega retained the right to inspect the vessels in drydock upon notification and at any other reasonable times to inspect the vessels and their logs. Union has complied with the requirement that it pay monthly charter hire in New York funds by writing checks in California drawn on New York banks where funds deposited for such purposes are available for Cienega's convenience.

The case raises the basic issues whether the trial court properly found: (1) a taxable "use" of these vessels occurred in California subsequent to their sale; (2) the purchaser (Cienega) contemplated, at the date of such transfer, the essential condition of such "use"; (3) the statute itself did not exempt from taxation Cienega's use of the property, and (4) California did not violate any constitutional prohibition in imposing the tax. We set forth in the above sequence our reasons for concurrence with the trial court.

In analyzing the first issue, we shall point out that the statutory definition of "use" includes the owner's use of the property by means of leasing it, and that, further, such an interpretation accords with the statutory design that the use and sales taxes be interpreted as complementary taxes.[2]

The statutory definition of "use" includes that exercise of dominion over property which takes the form of leasing it. The definition reads: " 'Use' includes the exercise of any right or power over tangible personal property incident to the ownership of that property, except that it does not include the sale of that property in the regular course of business." (Rev. & Tax. Code, § 6009.) The lease is an articulation of that right incident to the ownership of the property. Ownership is not a single concrete entity but a bundle of,

2. Relevant sections of the statute provide:
Rev. & Tax. Code, § 6201: "An excise tax is hereby imposed on the storage, use, or other consumption in this State of tangible personal property purchased from any retailer . . . for storage, use, or other consumption in this State. . . ." Rev. & Tax. Code, § 6202: "Every person storing, using, or otherwise consuming in this State tangible personal property purchased from a retailer is liable for the tax. . . ." (See J. Gould, The Calif. Tax System, 59 West's Ann. Cal. Codes, p. 51.)

rights and privileges as well as of obligations.[3] It finds expression through multiple methods. One such method is the lease. And where the owner physically uses the leased property, there, indeed, the ownership is exerted. When the tankers enter California the owner continues the exertion of its right of ownership through the instrument of the lease; the owner "uses" the tankers in California. The taxing authority at the location where the owner expresses or exercises such ownership may properly find that such use constitutes a taxable use.

The statutory definition recognizes that the term "use" covers the utilization of property for profit-making purposes by means of leasing; the word "use" is by no means restricted to physical manipulation. Thus Webster's New Twentieth Century Dictionary (1950) states as one of the meanings of the word, The act of handling or employing in any manner, and for any purpose, but especially for a profitable purpose; the state of being employed; employment; application; conversion to a purpose; . . . Likewise, a Kansas court, in defining the word and describing the extent of a bequest of property in trust "for *the use* and benefit" of the mother of a testatrix, holds: "'As a general rule, the use of a thing does not mean the thing itself, but means that the user is to enjoy, hold, occupy, or have in some manner the benefit thereof. If the thing to be used is in the form or shape of real estate, the use thereof is its occupancy or cultivation, etc., *or the rent which can be obtained for its use*. If it is money or its equivalent, generally speaking, it is the interest which it will earn.' 29 A. & E. Ency. of

3. Henneford v. Silas Mason (1937) 300 U.S. 577, 582; Superior Bath House Co. v. McCarroll (1941) 312 U.S. 176, 180-181; In re Hunter's Estate (Mont. 1951) 236 P.2d 94, 99; U.S. v. Gossler (D.C. Ore. 1945) 60 F. Supp. 971.

Law, 444." (Elwell v. Stewart (Kan. 1922) 203 P. 922; emphasis added.)

Our interpretation finds corroboration in section 6201, which imposes the use tax upon "storage, use, *or other consumption*" in this state. As the court in In re Los Angeles Lumber Products Co. (D.C. S.D. Cal. 1942) 45 F. Supp. 77, has said in regard to the use tax, ". . . not only 'use' but also 'storage' or 'other consumption' is taxable under the Use Tax Act." (P. 82.) The word "consumption" encompasses a gradual "using up or wearing away of something" (Webster's Third International Dictionary); to the extent that a deterioration, even though imperceptible, occurred in California, "consumption" of the vessels ensued. The tax applies to "all consumers" (Traynor, The California Use Tax (1936) 24 Cal. L. Rev. 175, 177), including the gradualist consumer.

The words "other consumption" are supplementary, not surplusage, to the remaining words of the section (Weber v. County of Santa Barbara (1940) 15 Cal. 2d 82, 86) and "significance should be given" to them (Select Base Materials v. Board of Equalization (1959) 51 Cal. 2d 640, 645). The vessels were actually used in California; here, too, the consumption as well as the use, took place.

The concept that Cienega used and consumed the vessels in California effectuates the basic purposes of the use tax and the broad statutory construction which we must accord its provisions.[4] As we stated in Chicago Bridge and Iron

4. Our construction of statutory terminology must rest upon the legislative objectives; these we are bound to effectuate. (Select Base Materials v. Board of Equalization (1959) 51 Cal. 2d 640, 645; San Francisco v. San Mateo (1941) 17 Cal. 2d 814, 818.) We note that the legitimacy of the use tax goal has been recognized by the United States Supreme Court: "The Use Tax Act is complemental to the California Retail Sales Tax Act of 1933. The latter levies a tax upon

Co. v. Johnson (1941) 19 Cal. 2d 162, 165: "One of these purposes is to make the coverage of the tax complete to the end that the retail sales tax . . . will not result in an unfair burden being placed upon the local retailer engaged solely in intrastate commerce as compared with the case where the property is *purchased for use* or storage in California and is used or stored in this state. The two taxes are complemental to each other with the aim of placing the local retailers and their out-of-state competitors on an equal footing." (Emphasis added; see also Brandtjen & Kluge v. Fincher (1941) 44 Cal. App. 2d Supp. 939, 941-942, and Traynor, The California Use Tax (1936) 24 Cal. L. Rev. 175, 176-177.)

If the California businessman, intending to buy property for use in California, could avoid the sales tax merely by purchasing the product outside the state, the local retailer would suffer a severe commercial disadvantage. Hence California imposes an excise tax upon the purchaser of tangible personal property in the event that, having paid no sales tax to California on the purchase, he proposes to and actually does store, use, or otherwise consume such property in this state.

In substance, the sales and use tax laws constitute a double filter designed to catch all transactions which result in tangible personal property joining the aggregate of capital assets within this state. In modern commercial practice capital assets available for lease compete with those avail-

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the gross receipts of California retailers from sales of tangible personal property; the former imposes an excise on the consumer at the same rate for the storage, use or other consumption in the state of such property when purchased from any retailer. As property covered by the sales tax is exempt under the use tax, all tangible personalty sold or utilized in California is taxed once for the support of the state government." (Southern Pacific Company v. Gallagher (1939) 306 U.S. 167, 171.)

able for ownership.[5] As we have explained, the Legislature designed the Sales and Use Tax law as an integrated whole. Such a design is incompatible with an interpretation of the statutes which would leave a loophole of competitive advantage for the interstate over the intrastate lessor. The use tax, correctly applied, constitutes a legitimate expense exacted for the privilege of enjoying the advantages of the California economy.

Cienega thus becomes the owner and consumer of property which it uses to produce rental income. In terms of the sales tax laws the sale to it would be a taxable sale. An equivalent result should occur as to the tax liability under the use tax laws: "[W]hen a person buys property in one state for the purpose of leasing it and transporting it to a person in another state where a use tax law is in effect, the lessor is considered as using the property in the second state for the production of income and hence is subject to such state's use tax even though he personally makes no physical use of the propery in such state." (Keesling, Conflicting Conceptions of Ownership in Taxation (1956) 44 Cal. L. Rev. 866, 867.)[6]

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5. Business enterprises have traditionally acquired operating machinery and equipment by purchase. Only in recent years has the field of industrial equipment leasing expanded to the magnitude of a billion dollar industry as attested by current articles featured in legal and financial publications. See, e.g., Equipment Leasing (Spring, 1962) University of Illinois Law Forum, 1-97; "Leasing Equipment is Big Business Today," Magazine Wall Street, Vol. III, Issue 1, Sept. 22, 1962, p. 33; "Equipment Leasing Now Big Business," Financial World, Vol. 117, Issue 19, May 9, 1962, p. 6; "Machines Without Owners," Fortune, Vol. 66, Issue 2, August, 1962, p. 112; "More Firms are Leasing Equipment," The Office, Vol. 58, Issue 2, August, 1962, p. 166.

6. As Union points out, Mr. Keesling advocates, in two footnotes, that a lease should be treated as the sale of a portion of ownership interest. Then either the lessor would pay a sales tax upon gross rental receipts or the lessee would be required to pay a use tax upon the rental price. As we later point out in the text, the Legislature

Having determined that Cienega used the property in California and that the transaction under the sales tax laws would be a taxable sale, we believe that the state properly assessed the use tax upon the sales price which the purchaser paid for the vessels. Although Union has suggested at oral argument that if any use tax were at all to be levied it should have been based upon the rental value of the property, we shall briefly explain why the tax must be imposed upon the purchase price of the vessels.

The use tax does not depend upon the *duration* of the use in California but upon the *fact* of *any* substantial use in California.[7] Since the rental value is not the controlling factor, the actual length of the lease and the rental payments are immaterial. The tax impinges upon Cienega's purchase *for* California use. (Rev. & Tax. Code, § 6201.)

As we have explained, the use tax takes the place of the sales tax in order that retailers who sell products in California will not be placed at a disadvantage as compared to those who buy products for use in California. In the case of the sales tax we are not concerned with the buyer's disposition of the product. The purchaser of a car in Cali-

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did not adopt this "divisible" theory of ownership but followed the opposite approach, specifically excluding as to sales taxation liability for most lease transactions. Mr. Keesling acknowledges this fact, but suggests that the "divisible" theory should nonetheless apply to subject the lessee to liability for a use tax. This proposal conflicts with the synchronized operation of California's sales and use tax system.

7. The tax is imposed when the evidence fairly demonstrates that the purchaser of the property contemplated a prompt and substantial employment of the property in California. The State Board of Equalization applies the "principal use" test and imposes the tax only if the item is used principally in this state during the initial year or six months following its purchase under circumstances which reveal that it was purchased for that purpose. (See Sales Tax Counsel Ruling of January 10, 1955, CCH State Tax Reporter, California, Vol. 2, paragraph 60-180.723.)

fornia, for instance, may sell it the next day or may keep it for ten years; in either event, he pays the sales tax upon the whole purchase price. In like fashion, the purchaser who buys the car outside of California for use in California by leasing it here pays his use tax upon the purchase price of the car.

These considerations, we believe, compel the conclusion that Cienega used, and exercised control over, the property in California, consumed it here, and is taxable upon the purchase price. Nor is this conclusion affected by Union's two opposing contentions that: (1) we should adopt the rationale of the Supreme Judicial Court of Maine in rejecting the taxation of a purchaser-lessor under similar use tax statutes, and (2) we should apply the "divisible property" theory which this court has recognized in imposing ad valorem taxation of real property leases.

Union urges, first, that we follow the decisions of the Supreme Judicial Court of Maine, the only other appellate jurisdiction which has adjudicated a similar issue. In two cases which construed the application of Maine's comparable statutes to an out-of-state lessor's purchase of tangible personal property for the lessee's physical operation within Maine, the court held that only the lessee's activity constituted a "use" within the state. (Trimount Coin Machine Co. v. Johnson (Me. 1956) 124 A. 2d 753; South Shoe Machine Co., Inc. v. Johnson (Me. 1963) 188 A. 2d 353.) "The use and *possession* of the property in Maine in its entirety is, and at all times has been, in the lessee or customer by virtue of the lease." (Trimount Coin Machine Co. v. Johnson, supra, p. 755; emphasis added.)

As we have stated, supra, the concept of "use" as mere physical manipulation overlooks all the other attributes of ownership, *including the incident of leasing;* it is arbitrarily

restrictive and academic. The Maine court has itself somewhat retreated from the rigid approach exemplified by these cases, holding in Automatic Canteen Company of American v. Johnson (Me. 1963) 190 A. 2d 734, that if the lessor of automatic vending machines, which were used in the state, dispatched its employees into the state to check upon the machines, the "acts" of the lessor constituted sufficient use to justify the imposition of the use tax. In any event, the Maine legislature revised its use tax statutes specifically to impose a use tax upon the rental of property within the state. (Me. Rev. Stats., ch. 17, § 4-B, added by P.L. 1961, Ch. 58.)

Union, in an attempt to equate use with physicial use, urges that we apply here the divisible theory of ownership, which determines the imposition of ad valorem taxes upon real property. As we shall show, however, the argument ignores the respective objectives of the use tax and the ad valorem tax.

The use tax "does not fall upon the owner because he is the *owner*, regardless of the use or disposition he may make of the property. It is imposed on certain of the *privileges* of ownership, but not on all of them." (Douglas Aircraft Co., Inc. v. Johnson (1939) 13 Cal. 2d 545, 551; emphasis added.) The use tax frames an excise tax upon the privilege of utilizing property within this state in a certain manner. "A privilege tax . . . is imposed upon the right to exercise a privilege, and its payment is invariably made a condition precedent to the exercise of the privilege involved." (Ingels v. Riley (1936) 5 Cal. 2d 154, 159.) The sales and use taxes encompass apposite privileges. "A sales tax is a tax on the freedom of purchase. . . . A use tax is a tax on the enjoyment of that which was purchased." (McLeod v. Dilworth Co. (1944) 322 U.S. 327, 330.)

The provisions of the Sales and Use Tax Law demonstrate that the Legislature did not adopt for those taxes the divided ownership theory. That theory conceives of the lease as a transfer of part of the "ownership" upon delivery of the property. Hence during the term of the lease the lessor cannot be the owner of "tangible personal property" which he could "use." Yet the Revenue and Taxation Code, section 6006, as to the sales tax, rejects the divisible property theory, providing that bona fide lease transactions are *not* to be considered "sales." Section 6006 and section 6009, which defines use, comprise part of chapter 1 of the same statute and apply to the identical scheme of taxation. We cannot conceive that, despite the complementary composition of the taxes, the Legislature meant to enact the divided ownership theory for the use tax but not for the sales tax.

A different approach, expressing different basic legislative intendments, underlies the decisions in regard to the taxation of real property. Although privately-held leasehold interests in publicly-owned real property are subject to taxation, the public ownership interest is exempt (Texas Co. v. County of Los Angeles (1959) 52 Cal. 2d 55); the rental price, moreover, is considered the purchase price of the leasehold interest and, for purposes of appraisal by the capitalization of net income method, the rental is not deductible as an expense. (DeLuz Homes, Inc. v. County of San Diego (1955) 45 Cal. 2d 546.)

In a similar fashion a school district's leasehold interest in privately-owned real property gains exemption from taxation since the property is "used exclusively" for public school purposes. (Ross v. City of Long Beach (1944) 24 Cal. 2d 258.) In *Ross* this Court effecuated the divisible property concept in interpreting constitutional provisions

which exempted two classes of property: (1) property "*used exclusively*" for specified public purposes, and (2) property "*belonging*" to a government body. In rejecting the argument that for purposes of property taxation the private owner in leasing his property "uses" it commercially and hence the property is not "used *exclusively*" for school purposes, we said, "To so construe the constitutional provision would tend to eliminate the main distinction between the two classes of property enumerated therein. In order to so construe this provision of the Constitution it would be necessary to insert therein the words 'which may belong to a school district' or words of similar import, so that the clause respecting property used for public school purposes would read 'property which may belong to a school district and used exclusively for public school purposes.' To insert these suggested words into this section of the Constitution would give to it an added meaning not to be found in the definite language of the section as adopted by the people . . . ." (Ross v. City of Long Beach (1944) 24 Cal. 2d 258, 260.)

The requirement for a narrow construction of "use" in order to integrate it with the balance of the statute, as occurred in *Ross*, contrasts with the considerations here which call for the opposite result. The statutory scheme here induces a liberal interpretation of the word use in order to achieve consistency with the sales tax. Additionally, the rule in ad valorem tax legislation which recognizes the concept of separate taxation of possessory interests relates to real property (General Dynamics Corporation v. County of Los Angeles (1958) 51 Cal. 2d 59, 65) and even in that coverage pertains to a limited area.

Thus the sales and use tax statutes presently and consistently express in definition and design the indivisible

ownership theory. To interpose by judicial fiat a contradictory concept in the administration of the use tax would be to create a breach in our comprehensive revenue system.

We now undertake an analysis of the second issue set forth above: whether Cienega purchased the vessels for the purpose of storage, use and consumption in California. We shall explain why we have concluded that the record supports the trial court's finding that the vessels "were purchased for use and consumption in the State of California."

This court has expressly held that products are purchased for use in California if at the time of sale, the lessor contemplated that the products would be used in this state. (Chicago Bridge & Iron Co. v. Johnson (1941) 19 Cal. 2d 162.) While that use may have been only a matter of the anticipated probabilities at the time of the purchase, once the probabilities congeal into particular events constituting a "use" within the state, the transaction becomes taxable. (Atchison etc. Ry. Co. v. State Board of Equalization (1956) 139 Cal. App. 2d 411; Flying Tiger Line v. State Board of Equalization (1958) 157 Cal. App. 2d 85.) Other jurisdictions have reached a similar conclusion. (See Morrison-Knudsen Co. v. State Tax Commission (Iowa 1950) 44 N.W. 2d 440, Annot., 41 A.L.R. 2d 535; Western Contracting Corp. v. Iowa State Tax Commission (Iowa 1961) 112 N.W. 2d 326.) When the use contemplated by the lessor is, in fact, effectuated following the transfer, the obligation matures; the duty of collecting the tax becomes the retailer's.

If the parties transfer title outside of the state but the lessor entertains the expectation of California use, which is later fulfilled, the locus of the sale or delivery does not control the issue. Of course, the taxpayer may show as a matter of defense the payment of the California sales tax.

"The use tax applies to property purchased for use in this state wherever purchased, unless the gross receipts from the sale have been included in the measure of the California sales tax (Rev. & Tax. Code, § 6401), or unless the transaction is otherwise exempted by the statute or by the state or federal Constitution." (Flying Tiger Line v. State Board of Equalization (1958) 157 Cal. App. 2d 85, 98.) Indeed, California enacted a use tax so that the taxability of property purchased for use in this state, and principally used thereafter in this state, should not turn upon the fortuity of whether or not title or physical delivery of the property passed within this state. (Traynor, The California Use Tax (1936) 24 Cal. L. Rev. 175.)

In this case both parties to the transaction, Union and Cienega, knew that the vessels had been employed principally in California intrastate commerce for a considerable period immediately prior to the transfer. The parties at the date of the transaction did not anticipate a change in operations; they entertained a contrary, if unexpressed, intention. Subsequent to the transfer the vessels were indeed used in the same manner as before; both before and after the transfer Union employed these vessels a minimum period of approximately 70 per cent of each year in intrastate activities. We do not suppose that Cienega, as the purchaser and lessor, would execute bareboat charters concerning two vessels valued at nearly $5,000,000 without some fairly reliable information as to the manner and locale of their subsequent employment. We find substance in the trial court's conclusion that Cienega must have contemplated that the ships would be returned to, and operated within, California.

Once this inference arises as to Cienega's expectation, the burden of rebuttal falls upon the plaintiff, Union, in California; yet Union has failed to meet that burden. (See

El Dorado Oil Works v. McColgan (1950) 34 Cal. 2d 731, 744; Pacific Fruit Express Co. v. McColgan (1944) 67 Cal. App. 2d 93, 96.) Union presented no affirmative evidence to rebut the inference that Cienega contemplated that the vessels would be operated under the lease in California.

Yet Union, as both retail seller and lessee of the vessels, occupied a position of peculiar knowledge as to the information afforded Cienega as to the past and present use of the vessels. The record, however, contains neither evidence that the parties proposed to change the way the vessels were to be utilized nor that the vessels were not utilized in precisely the manner which was anticipated. In any event, Union, as the retailer, under California law becomes the state's involuntary tax collector and cannot, in this instance, complain that injustice to it accrues from its lack of knowledge of the known conditions which created its obligation to collect the tax.

Turning now to the third issue suggested, supra, we point out that California may properly impose upon Union the duty to collect this tax since Cienega's use of the property gained no exemption upon statutory grounds.

Although Union relies upon section 6368 of the Revenue and Taxation Code, which expressly exempts from sales or use taxation watercraft "for use in interstate or foreign commerce involving the transportation of property or persons for hire," this section does not apply here. As we shall explain, in the first place, the lessor did not use the vessels for transportation of property or persons "for hire"; in the second place, the lessor did not employ the vessels, themselves, primarily in interstate or foreign commerce.

Cienega leased the vessels to Union; Cienega did not arrange for the transportation of property for hire; the phrase "for hire" in the statute relates to the property or

goods carried and not the vessel which hauls the goods. Union employed the vessels, moreover, principally in intrastate operations. By virtue of a formal ruling by the State Board of Equalization (Ruling 51.5, 18 Cal. Admin. Code, § 1992) this exemption does not apply to the principal use of the vessels in intrastate operations.[8] The instant ruling embodies a reasonable interpretation of the statute; such a valid classification will be followed by this court. (General Electric Co. v. State Board of Equalization (1952) 111 Cal. App. 2d 180, 188.)

Our fourth and final issue involves the constitutionality of California's exaction of the tax. Because Cienega enjoyed the use of its tangible property in California, California may properly impose a tax upon that privilege. We have explained that Cienega, by means of leasing the vessels, used them in this state; the cases hold that California's taxation of that utilization of the property does not violate the due process clause of the Fourteenth Amendment.

The due process clause requires "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." (Miller Bros. Co. v. Maryland (1954) 347 U.S. 340, 344-345.) The state's action will satisfy the constitutional test "if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society." (Wisconsin v. J. C. Penney Co. (1940) 311 U.S. 435, 444.) The

8. "While this contemporaneous administrative construction is not necessarily controlling, it 'is entitled to great weight, and courts generally will not depart from such construction unless it is clearly erroneous or unauthorized.' (Coca-Cola Co. v. State Board of Equalization, 25 Cal. 2d 918, 921 . . . .)" (Select Base Materials v. State Board of Equalization (1959) 51 Cal. 2d 640, 647; see also Anders v. State Board of Equalization (1947) 82 Cal. App. 2d 88, 98.)

instant situation displays "the link": the use of the vessels impinged in California; California granted to them the benefits of an ordered society.

Not only may the state impose an ad valorem tax upon the nonresident owner for a chattel located in the taxing state; it may also levy upon such an order a tax upon the profits of a sale of the property in the taxing state. Thus the decisions of Coe v. Errol (1886) 116 U.S. 517, and Pullman's Palace Car Co. v. Pennsylvania (1891) 141 U.S. 18, establish the constitutionality of such an ad valorem tax. The ruling in New York ex rel. Whitney v. Graves (1937) 299 U.S. 366, 369, holds that the "profits realized by a nonresident upon the sale of a right appurtenant to membership in the New York Stock Exchange" could properly be taxed by New York. The state may thus tax the out-of-state owner, represented by Cienega here, for the earnings derived from property in the taxing state.

A decision of the Supreme Court of Mississippi, in which the United States Supreme Court dismissed an appeal and refused a hearing, passes upon this exact issue. In Stone v. Stapling Machine Co. (Miss. 1954) 71 So. 2d 205, a foreign corporation rented its machines to Mississippi lessees in New Jersey for use in Mississippi: ". . . these machines were carried to Mississippi but they remained the property of the company." (P. 207.) The court found no violation of due process in the imposition of the state's sales tax upon the rental receipts. Since the California sales tax law does not include bona fide leases within the definition of "sale" (Rev. & Tax Code, § 6006, subd. (a)) but holds the lessor to be the consumer of the property, the tax involved in the Mississippi case would have been labelled a use tax here. The nomenclature of the tax does not affect the principle of the holding of tax liability.

Finally, the cases cited by Union in negation of the state's constitutional power to tax do not exactly apply to the instant situation. Its reliance upon Miller Bros. Co. v. Maryland, supra, 347 U.S. 340, and Scripto v. Carson (1959) 362 U.S. 207, overlooks the fact that both of those cases recognize the distinction between the out-of-state transaction which embodies the owner's outright sale of the property, severing his connection with it, and the owner's lease of the property for use in the taxing state. *Miller* involved cash sales to customers, some of whom bought for Delaware use, which Delaware sought to tax. Yet as the Supreme Court noted in *Scripto* ". . . it was impossible for Miller to determine that goods sold for cash to a customer over the counter at its store in Delaware were to be used and enjoyed in Maryland." (P. 212.)

In the instant case Cienega anticipated Union's use of the vessels in California. Our case more closely resembles *Scripto*, a situation in which Florida levied a tax upon the out-of-state seller "for use and enjoyment of property which has been purchased by Florida residents." (P. 211.)

The imposition of the use tax, as we shall now explain, clearly does not unduly burden interstate commerce. We can no longer question the constitutionality of the complementary use tax as an undue burden upon interstate commerce as such; Henneford v. Silas Mason Co. (1936) 300 U.S. 577, settled the issue: "The tax is not upon the operations of interstate commerce, but upon the privilege of use after commerce is at an end" (p. 582); "The tax upon the use after the property is at rest is not so measured or conditioned as to hamper the transactions of interstate commerce or discriminate against them." (P. 583.)

Thus, so long as an appropriate "taxable interval" of intrastate enjoyment intervenes, the indirect effect upon

interstate commerce does not affect the constitutionality of the tax. (Southern Pacific Co. v. Gallagher (1939) 306 U.S. 167; Pacific Tel. & Tel. Co. v. Gallagher (1939) 306 U.S. 182.) Since in the instant case Union operated the two vessels in intrastate commerce in this state, the taxable interval occurred.

Nor does the use tax violate the inhibition of General Trading Co. v. State Tax Commission of Iowa (1944) 322 U.S. 335, 338, that "[T]he mere fact that property . . . has come into an owner's possession as a result of interstate commerce does not diminish the protection which he may draw from a State to the upkeep of which he may be asked to bear his fair share. . . . But a fair share precludes legislation obviously hostile or practically discriminatory toward interstate commerce." California levies its use tax with respect to property stored, used or consumed in this state at rates uniform with those imposed upon retail sales by the sales tax; it does not discriminate against interstate commerce but protects local retails from the discriminatory advantage which out-of-state competitors would otherwise enjoy. We see no constitutional violations in California's imposition of its use tax in this instance.

As to the transaction itself, we cannot, in the face of a showing that the parties contemplated the use of the property under the lease in California, apply the balm of tax immunity. The contract, consummated outside the state, provided theoretically for the use of the vessels in all states, but the formality of the phrase cannot block out the reality of the transaction. The facts of the arrangement demonstrate that the parties anticipated the use of the property in California; subsequent history confirms that use. If we hold that in these circumstances the technique of the extra-territorial sale and leaseback transaction wins

use-tax immunity, we invite a wholesale emigration of parties to other states for the consummation of such tax-saving contracts.

The judgment of the trial court is affirmed.

TOBRINER, J.

We concur:
GIBSON, C. J.
TRAYNOR, J.
SCHAUER, J.
PETERS, J.
PEEK, J.

Union Oil Co. v. State Board of Equalization—Sac. 7356

DISSENTING OPINION

I dissent. I would reverse the judgment for the reasons expressed by Mr. Justice Van Dyke in the opinion prepared by him for the District Court of Appeal in Union Oil Co. v. State Board of Equalization (Cal.App.), 28 Cal. Rptr. 58.

McCOMB, J.

Appendix

In the District Court of Appeal of the State of California

In and For the Third Appellate District—(Sacramento)

3 Civil No. 10382—(Sac. No. 7356)

Union Oil Company of California, a corporation,
Plaintiff and Appellant,

vs.

State Board of Equalization of the State of California,
Defendant and Respondent.

Filed: Jan. 29, 1963

OPINION

This is a suit for a refund of use tax. It arises out of the sale and subsequent use of two ships, the SS Santa Paula and the SS Lompoc. The two ships were sold by appellant to Cienega Tanker Corporation. The sale took place outside of California and was not subject to California sales tax. The state contended, however, that Cienega incurred California use tax liability on the theory that it purchased the ships outside of California, intending to use them in California and thereafter did so. The State therefore assessed use tax and interest in the sum of $151,800.00 and called upon appellant, Union Oil Company, the vendor of the vessels, to collect the tax and pay it over to the state pursuant to the provisions of sections 6203-6204 of the Revenue and Taxation Code which require a retailer maintaining a place of business in this state (as did Union) to collect any use tax due from those to whom it sells property

The facts are not in dispute and are contained in a stipulation of record.

Union Oil Company of California is a California corporation engaged in producing, refining, manufacturing, transporting, distributing and marketing petroleum and petroleum products. Its business activities extend throughout the United States and its territories, and into Canada, South America and other foreign countries. In connection with the distribution of its products, Union has for many years operated tank ships for the purpose of transportation to the various areas in which its refining and marketing facilities are located.

Cienega Tanker Corporation is a Delaware Corporation. Its principal office is in the City of Wilmington in that state, and Cienega is not, and never has been, qualified to do business in California. It does not do and never has done business therein nor does it have, nor has it ever had, any officers, representatives, agents, employees or other personnel in California.

On March 5, 1953, Union and Cienega entered into a contract of sale at Jersey City, in New Jersey, whereby Union agreed to sell to Cienega five bulk oil tankers, including the SS Santa Paula and the SS Lompoc. Union agreed to deliver each vessel to Cienega at Astoria, in Oregon, or such other port in the United States of America as Cienega should designate. Cienega agreed to pay for the vessels by cashier's or certified check, or checks in New York, funds. The purchase price of the SS Santa Paula and the SS Lompoc was $2,200,000 for each vessel.

The contract of sale provided that concurrently with the delivery of each vessel Union and Cienega would execute a bareboat charter party with respect thereto. Pursuant to this stipulation Cienega chartered the SS Santa Paula to

Union for a period of 24 months and the SS Lompoc for a period of 48 months with options granted to Union to extend each charter period for 12 months. The terms of each charter party required Union to pay charter hire to Cienega each month in New York funds and this has been done.

The SS Santa Paula was purchased and chartered pursuant to the above-described contract of sale on March 17, 1953. All documents of title, certificates, checks and other papers required for the sale were delivered and all documents necessary for the charter were executed and delivered in Jersey City, New Jersey, on that date. The vessel was delivered by Union to Cienega and redelivered by Cienega to Union in Astoria, Oregon, under charter on that same date. The purchase and chartering of the SS Lompoc were handled in the same fashion on March 20, 1953. Cienega has never given to Union any directions with respect to the places or areas in which Union should operate the vessels, and by the terms of the charters was without any right or authority to do so. Each of the charters contains the following provision relating to use and operation of the vessels:

> "Charterer shall have the full use of the Vessel and may employ the Vessel in any trade throughout the world, except that the Vessel shall not be operated in any manner contrary to applicable law and shall not carry any cargo that will expose the Vessel to penalty, forfeiture or capture."

The charters likewise permit Union "to subcharter the Vessel to others on a time or voyage basis."

The stipulated record of use of the two vessels during the year following the sale is as follows:

During the period from March 17, 1953 to March 17, 1954, the year immediately following its sale, the SS Santa Paula

was operated by Union outside the California three-mile limit for 145 days, within the three-mile limit for 188 days, and spent 32 days in dry dock.

During the period from March 20, 1953 to March 20, 1954, the year immediately following its sale, the SS Lompoc was operated by Union outside the three-mile limit for 142 days, within the three-mile limit for 198 days, and spent 25 days in dry dock.

The dry docking of the vessels occurred in California.

The Sales and Use Tax Law is found in Part 1 of Division 2 of the Revenue and Taxation Code. The use tax is imposed by section 6201, which provides:

> "An excise tax is hereby imposed on the storage, use, or other consumption in this State of tangible personal property purchased from any retailer on or after July 1, 1935, for storage, use, or other consumption in this State . . ."

Section 6202 provides, in part, that the primary liability for the tax is upon the purchaser:

> "Every person storing, using or otherwise consuming in this State tangible personal property purchased from a retailer is liable for the tax. . . ."

"Storage" is defined by section 6008:

> "'Storage' includes any keeping or retention in this State for any purpose except sale in the regular course of business or subsequent use solely outside this State of tangible personal property purchased from a retailer."

"Use" is defined by section 6009 as follows:

> "'Use' includes the exercise of any right or power over tangible personal property incident to the ownership of that property, except that it does not include

the sale of that property in the regular course of business."

The use tax is imposed upon a person who stores, uses, or otherwise consumes in this state tangible personal property purchased from a retailer for storage, use or other consumption in this state. It is undisputed that Cienega purchased the vessels from Union, a retailer. Therefore two questions are posed, one, did Cienega store, use or otherwise consume the vessels in California, and, two, did Cienega purchase the vessels for the purpose of such storage, use or other consumption? A negative answer to either or both of these questions necessitates reversal.

Contending that Cienega did not use the tangible personal property here involved in California, appellant argues as follows: The tax is imposed on the use of tangible personal property in California; the property in this case consisted of two ships which are things, that is, steel plates, engines, decks, etc.; the law specifically defines tangible personal property as "personal property which may be seen, weighed, measured, felt, or touched, or which is in any other manner perceptible to the senses." (Rev. & Tax. Code, sec. 6016.) From this premise appellant argues further that Cienega, after the delivery of the vessels to appellant under the charters, not only did not make, but under the charters had no authority or right to make, use of those vessels within the meaning of the word "use" as that word appears in the statutes, saying that "use" means statutorily the physical use of tangible personal property. If the statutory meaning of "use" is so limited, then, as appellant contends, once Cienega had, pursuant to the charters, delivered the vessels physically into the exclusive possession of appellant it neither did nor could during the charter period use the

property in California or elsewhere. Any such use of the property thereafter was necessarily and exclusively that of appellant.

Respondent insists that the interpretation of the word "use" cannot properly be limited as appellant would have it to the physical use of tangible personal property. Respondent does not contend that if the interpretation contended for by appellant be adopted, Cienega has made use of the vessels. Respondent argues that the employment of the ships in California for the production of income therefrom was a "storage, use, or other consumption" of the property by Cienega within the meaning of the statutes, regardless of the fact that the owner-lessor remained out of state. Says respondent, the leasing of property is the "exercise of a right or power over the property "incident to the ownership of the property" (this much is conceded by appellant).

In this controversy over the meaning of the word "use", appellant relies strongly upon Ross v. City of Long Beach, 24 Cal. 2d 258; 264. In that case a private party leased land and buildings to a school district and claimed that since the school district was in possession and was physically using the land and buildings exclusively for school purposes, the private owner was entitled to tax exemption under the Constitution. The city contended, as respondent contends here, ". . . that there is a further and additional use of said property than that for which the . . . [lessee] uses it, and that is the use by the . . . [lessor] who rents it for the purpose of deriving revenue therefrom" This argument that the owning of property and the holding of it for purposes of producing rental income was a use of the property, even though not a physical use thereof was rejected by the Supreme Court. The court distinguished between the own-

ership of property and the possession and use of it by the district for public school purposes, saying (at p. 265): "[W]e are in accord with the decisions of those courts in other jurisdictions, as well as in our own, which hold that it is the *use* and not the *ownership* of the property in the possession of a school district and used by it for public school purposes that determines its status as property exempt from taxation." The Supreme Court in Ross was construing Article XIII, section 1, of the Constitution and particularly the exemption from taxation contained therein, granting such exemption as to "property used exclusively for public schools." The decision is not conclusive here where the interpretation of the use tax law is involved, even though both cases are concerned with the use of property. Nevertheless, the theory of divisible use of property by lessor and lessee was presented in Ross and for the purposes of that case was rejected.

Certainly it is permissible to say that the owner of property leasing it out and delivering it into the exclusive possession of a lessee is making a use of it and this is true whether the property be land or personal property, that is, physical objects. But the sales and use tax are emphatically concerned with taxing the sale, use, storage and consumption of tangible personal property, that is, property which "may be seen, weighed, measured, felt, or touched, or which is in any other manner perceptible to the senses." (Rev. & Tax. Code, sec. 6016.)

It is not claimed that in the transactions occurring between appellant and Cienega anything was concealed, or that any secret and undisclosed purposes were effectuated.

Cienega purchased the vessels from appellant. They were delivered into Cienega's possession. This having been done, Cienega chartered them to appellant by bareboat charter

and, pursuant thereto and acting without the State of California, delivered them to appellant. Whether thereafter Union used the vessels in California or used them elsewhere, as it did the other three vessels, was neither the concern of Cienega nor in anywise the act of Cienega. Indeed, it did not concern Cienega that appellant should make or not make any use of the vessels. These things appear from and are the result of the charter parties executed between Cienega and appellant. They were ordinary transactions in respect of the operation of such ships upon the high seas. As we read the statutes involved, Cienega did not store or use the vessels in California.

Something more should be said concerning the contention of respondent that there was, at least, a consumption by Cienega of the vessels in this state. In support of this contention respondent argues that the word "consumption" is broad enough to include natural obsolescence and the ordinary wear and tear incident to the physical use of any physical object. But the statute clearly states that the other consumption which is taxed is akin to use and storage of tangible personal property. The principle of ejusdem generis ought to be applied here. We note that the statutes specifically define "storage" and "use" by the purchaser, but no specific definition of "other consumption" is attempted. Whatever the words "other consumption" may include, we are satisfied that they do not include anything done by Cienega to or with the vessels during that part of the charter period with which we are here concerned. Undoubtedly, the use of the vessels by appellant during that period may be said in some manner to have partially consumed the vessels in that all things are consumed by use. But such consumption as may have occurred must be related to, as it flows from, the use by appellant.

For the same reasons it cannot be said that the record here supports a conclusion that Cienega purchased the vessels with the intent to store, use or otherwise consume them in California. From the record the intent of Cienega in the purchase of the vessels was to do with them exactly what was done—bareboat charter the vessels to appellant.

The researches of counsel and of this court have not disclosed any decision of appellate courts that specifically decide the questions here presented, save one. In Trimount Coin Machine Co. v. Johnson (1956), 152 Me. 109, 124 Atl. 2d 753, the Supreme Court of Maine was presented with the questions we have here, under statutes such as ours and under facts not materially different. The Maine taxing authorities argued that where vending machines were newly purchased outside Maine and again outside Maine were leased and by the lessee brought into Maine and used, the lessor must pay a use tax thereon. The Maine court rejected the contention. We quote the pertinent part of that decision:

"The question, however, is not whether the machine is in use, within the ordinary meaning of the word, in Maine, but whether the petitioner is so using it within the meaning of the statute. The person taxable must be both a user and the purchaser at retail sale. The lessee in Maine is a *user* but *not* the purchaser and hence is not taxable. The petitioner is the purchaser. Thus the decision turns on whether there is 'use' in Maine by the lessor.

"In our view of the statute the petitioner is not liable for a use tax. The use and possession of the property in Maine in its entirety is, and at all times has been, in the lessee or customer by virtue of the lease. In the instant case, as we have seen, the lease is bona fide and is not 'in lieu of purchase.' The rental provided under the lease is therefore true rent for the use of the property.

"To lease property in ordinary meaning is to obtain the use and possession of property in return for rent. . . .

"If the petitioner exercises in this State any right or power incident to its ownership of the machine, the use tax is imposed. The tax does not rest upon the *sum total* of rights and powers incident to ownership, but upon *any* right or power. There is, of course, no use tax arising under any theory of the Act from the purchase of the machine outside of Maine or from the lease written in Massachusetts. Until the machine reached the State of Maine there was no action whatsoever within the State with respect to the property owned by the petitioner.

"From the agreed statement it appears that the petitioner has done nothing with respect to the machine within the State of Maine either before or since making the lease. We conclude, therefore, that the petitioner has not exercised in this State any right or power over the property within the statutory definition of "use'."

The judgment is reversed.

VAN DYKE, J.
pro tem

We concur:
SCHOTTKY, Acting P. J.
FRIEDMAN, J.

In the Superior Court of the State of California in and for the County of Sacramento

No. 113643

Union Oil Company of California, a corporation,
Plaintiff,

vs.

State Board of Equalization of the State of California,
Defendant.

OPINION

Facts

Plaintiff sues to recover back a $151,800.00 (including interest) Use Tax levied by defendant, measured by the purchase price of two vessels sold by plaintiff to Cienega Tanker Corporation (hereinafter called "Cienega") in 1953. The sale took place in New Jersey, delivery was in Oregon, and Cienega is not a California corporation, nor is it licensed to do business here. (And, unless the leasing of the vessels hereinafter mentioned can be said to be "doing business" in California, it is not actually engaged in business here.) There is no inter-connecting stock ownership or other relationship between plaintiff and Cienega. By agreement between them, made at the same time and place of the sales contract, plaintiff leased from Cienega and took delivery back of the vessels by a written bareboat charter party, under which plaintiff acquired full use of the vessels, could use them any place in the world although these vessels both before and after were used principally in California or on the high seas, but between California ports. Charter fees (rent) were payable in New York funds. Plaintiff is a re-

tailer maintaining a place of business in California and at all times possessed a retailer's sales tax permit.

Under the bareboat charter, the plaintiff furnishes officers, crew, supplies and victuals and under the terms of the charter party was required to repair, maintain, overhaul, clean and paint the vessels, drydocking them at least once in every 12 month period, and to keep them in such condition as would entitle them to highest classification and rating of the American Bureau of Shipping. Cienega was allowed to inspect the vessels at reasonable times.

At the time of this transaction, neither New Jersey, where the sale took place, nor Oregon, where delivery and redelivery was made, had a sales tax or use tax.

Statutes Involved

The laws which the Court is called upon to interpret are:

Revenue and Taxation Code Section 6201:

> "An excise tax is hereby imposed on the storage, use, or other consumption in this State of tangible personal property . . . for storage, use, or other consumption in this State . . ."

Revenue and Taxation Code Section 6202:

> "Every person storing, using, or otherwise consuming in this State tangible personal property purchased from a retailer is liable for the tax. . ."

Revenue and Taxation Code Section 6203:

> "Every retailer maintaining a place of business in this State and making sales of tangible personal property for storage, use, or other consumption in this State . . . shall, at the time of making the sales or, if storage, use or other consumption . . . is not then taxable hereunder, at the time the storage, use, or other con-

sumption becomes taxable, collect the tax from the purchaser . . ."

Revenue and Taxation Code Section 6204:

"The tax required to be collected by the retailer constitutes a debt owned by the retailer to this State."

Revenue and Taxation Code Section 6008:

"'Storage' includes any keeping or retention in this State for any purpose except sale in the regular course of business or subsequent use solely outside this State of tangible personal property purchased from a retailer."

Revenue and Taxation Code Section 6009:

"'Use' includes the exercise of any right or power over tangible personal property incident to the ownership of that property, except that it does not include the sale of that property in the regular course of business."

The Questions

Broadly stated, the question is whether the out-of-state purchase of personal property to be let out for hire under an out-of-state lease without stipulation as to place of its use, but which is actually used in California, constitutes a taxable purchase for California "use or other consumption" *by the lessor* under the terms of the above quoted code sections.

The general question thus posed raises certain specific sub-questions which have been argued in the briefs and will be discussed under the separate captions below.

1. *Does Utilization of the Leased Vessels Constitute a "Use or Other Consumption" by Lessor In California?*

Plaintiff argues that it does not. It argues that since both the sale and the lease back were made out of California, with rentals paid out of California, mere permission to the lessee to use the leased property in California does not constitute a use (or their consumption) of the property by lessor who was the purchaser. (And, by the express provisions of the statute, the use tax must be predicated upon a use by the purchaser of the property although the seller-retailer is made the collector of the tax.)

Both parties concede that the question is one of first impression in California.

Plaintiff, however, relies upon the case of *Trimount Coin Machine Co. v. Johnson* (*Maine*, 1956), 124 A.2d 753. There, in an action for declaratory relief, a Massachusetts petitioner had purchased coin operated machines for the purpose of distributing or leasing them out for use by lessees or purchasers elsewhere. Those involved in this litigation were distributed to Maine lessees under bona fide leases made in Massachusetts, with rentals paid in Massachusetts, and with the machines delivered either in Massachusetts or sent on the lessees' orders f.o.b. Boston. Excepting that in some instances petitioner's salesmen had solicited the leases, in Maine, the transactions were unconnected with Maine—excepting that the machines were used there.

Preceding the Court's holding is its statement:

> "The decisive issue is whether the petitioner has exercised in this State any right or power over the machine described in the agreed statement incident to its ownership."

The Supreme Judicial Court of Maine held that it had not. It said (on p. 755):

> "In our view of the statute, the petitioner is not liable for a use tax. The use and possession of the property in Maine in its entirety is, and at all times has been, in the lessee or customer by virtue of the lease . . . The rental provided under the lease is therefore true rent for the use of the property.
>
> "To lease property in ordinary meaning is to obtain the use and possession of property in return for rent . . ."

The Court states further (on p. 756):

> "From the agreed statement it appears that the petitioner has done nothing with respect to the machine within the State of Maine either before or since making the lease. We conclude, therefore, that the petitioner has not exercised in this state any right or power over the property within the statutory definition of 'use'."

(The court did not pass upon constitutional questions raised by Petitioner.)

I can make no distinction between the facts of the *Trimount* case, and this, nor between the terms of the statute there being interpreted and California's Use Tax Law—and defendant has suggested none. Being a decision of the highest appellate court of Maine, it is—under the rule of stare decisus—persuasive (13 Cal. Jr. 2d 687). It is not, however, binding upon me, if I cannot agree with its logic, and, in this instance, I cannot.

I cannot agree that there can only be a use of leased property by either the lessor or lessee, but not by both at one time.

I cannot agree that a lessor who buys property for the specific purpose of leasing it out to another is not "using" it. More particularly, I cannot agree that such lessor is not "consuming" the property. Still more particularly, I can not rationalize a view that such a lessor is not exercising "any right or power over the machine incident to its ownership." To me, the vice of the Court's holding in the *Trimount* case (and the vice of the position expressed by plaintiff here) is that it considers "use" or "consumption" as synonymous with possession. The *Trimount* decision states:

> "The use and possession of the property in Maine in its entirety is . . . in the lessee . . ."

Possession, yes, but use no. Of course, the lessee *does* use the property. But cannot both lessor and lessee be said to be using it? Does not the owner of property held for rental use the rental property which it lets for hire just as literally as does the renter? Webster's Dictionary definition of the word, "use," includes:

> "The act of handling or employing in any manner, and for any purpose, but especially for a profitable purpose; the state of being employed; employment; application; conversion to a purpose."

Nothing in this definition presupposes physical possession as a necessary concomitant of use. And, if there can be any doubt of the utilization by a lessor constituting a "use," is there not most certainly a "consumption?"

Bringing the terms back into context, does not such use and consumption come within the broad purpose for which the Use Tax was designed? How else can the California business man be protected against his competitor?

Suppose that at King's Beach on Lake Tahoe in California, X is engaged in the business of renting out his trucks to the general public, but principally to California renters. In competition with him is Y whose customers operate in the same area; But Y's place of business is at Cal Neva just across the line in Nevada. Most certainly X must pay California's Sales or Use Tax regardless of whether he buys his trucks in Detroit or in California. Is Y to escape through the fortuitous circumstance that his place of business is across the state line although he derives his profits from California custom and thereby enjoys the benefits and protection which justify California taxation?

The illustration given above is, of course, not the typical one given as the reason for the complementary enactment of the Use Tax. The classic illustration shows it as a protection for the California retailer who must pay a sales tax on tangible personal property against the competing retailer in a sales-tax-free state selling to California customers (*Southern Pacific Co. v. Gallagher*, 306 U.S. 167, 171; *Chicago Bridge & Iron Co. v. Johnson*, 19 C.2d 162, 165). However, I see no lesser necessity to extend the protection to California lessors in the business of leasing personal property who must pay sales or use taxes upon the items which are their stock and trade against their out-of-state rivals competing for California customers.

As stated in *Chicago Bridge & Iron Co. v. Johnson* (1941), C.2d 162, the fundamental aim of the legislation is that "all tangible personalty sold or utilized in California is taxed once for the support of the state government," and this being so, use by out-of-state lessors who let their personalty to California customers justifies a tax to support state government just as much as use by California lessors.

(2) *Was This A Purchase FOR Use in California?*

Plaintiff argues that even assuming that he who lets out personalty for hire is using or consuming the property still Cienega under the facts here did not purchase these ships FOR use in California which is a condition to the imposition of the tax under Revenue and Taxation Code Section 6201.

Plaintiff says that it was neither stipulated in the contract between plaintiff and Cienega that the ships were to be used in California, nor were they in fact used here all of the time (although they have been in fact used by plaintiff either in California or on the high seas between California ports, principally both before and after the transaction).

Both parties have cited *Chicago Bridge & Iron Co. v. Johnson* (1941), 19 C.2d 162, a case which interprets the meaning of "for storage, use or other consumption in this State" as the phrase is used in Revenue and Taxation Code Section 6201. There, plaintiff was a Chicago tank manufacturer which purchased its raw materials and manufactured its tanks, all out of California, "knocked down" the product and reassembled them using skilled employees of its own on the premises of its customers who were in several states including California. During the period involved in the case, $161,000.00 in raw materials were purchased outside California expressly for manufacturing tanks to be erected in this State, and $70,000.00 in raw materials were taken from plaintiff's stock purchased for use anywhere as its business might require and used in tanks which were installed in California.

Regarding the point under discussion, the Court states (on p. 168):

> "It cannot be doubted that those materials which were purchased by plaintiff to fabricate tanks specif-

ically to fulfill contracts or orders for tanks in California, were purchased for use, storage or other consumption in this state . . .

"In regard to the portion of materials purchased by plaintiff and retained as stock in its plants . . ., it is clear that in order that the object and purpose of the Use Tax Act may not be frustrated, it must be concluded that they are subject to the use tax. Those materials were purchased for use, storage or other consumption in this state. While it is true that they were not acquired with the express purpose of performing any specified contract or order, plaintiff was engaged in the business of selling and constructing tanks in California. In the course of its business those materials might be used in California or elsewhere. It cannot be said therefore that they were not purchased for use here. They were purchased for use in California if and when the business required their use here to fill an order. The requirement arose and they were used in this state. It follows that those particular materials were purchased for use in California."

The distinction between the *Chicago Bridge & Iron* case, and this case, is that here it is the seller of the personalty (due to the circumstance that the lessee is also the seller) and not the purchaser (lessor) who determines where the property is to be used. But does this make the transaction any the less one where the purchase is "for use" in this State—especially where the seller is made liable to collect the tax? Does it make any difference whether the lessor or the lessee brings the property into the State? Here, again, I do not think so. Moreover, it seems to be implicit in this sale and lease back that these ships would be used principally in California or between California ports which to

my mind is the same thing since, as defendant argues, the ships derive no taxable benefits from the high seas. Also, it does not seem realistic, assuming as we must a bona fide transaction, that Cienega would lease five ships with a valuation approaching $10,000,000.00 under a bareboat charter without some pretty definite information, both as to manner of use and locale. But, regardless of this, plaintiff, who under California law is made the state's involuntary tax collector, cannot appeal to the court's conscience claiming injustice arising from lack of knowledge of the existence of the condition which created its obligation to collect the tax.

(3) *Does This Transaction Fall Within Watercraft Exemption Involving Transportation of Property for Hire?*

The contention of plaintiff in this regard is that if Cienega in letting these vessels out to plaintiff under a bareboat charter can be said to be "using" them within the terms of the Use Tax, then it was so using them "for hire" thus bringing the case within the Watercraft exemption of Revenue and Taxation Code Section 6368.

While this meaning is a literal possibility, I do not think the section can be so construed in context. It seems rather clear that the phrase "for hire" relates to the property or goods carried and not the carriage or vessel which hauls the goods.

(4) *Is This Use Exempt Under Revenue and Taxation Code Section 6352 and/or the Commerce Clause of the U.S. Constitution?*

Plaintiff does not claim that the Commerce clause is violated under the facts of this case. Rather, its claim is that if the Use Tax is interpreted to permit the tax here, then another set of facts can be imagined which *would* invalidate

the tax under the Commerce clause. The imagined facts are these: A freight car owner leases it to a railroad for use in interstate commerce. Being so used, it travels through 20 states, some or all of which levy a use tax, this resulting in multiple taxation.

The Court is not called upon to, nor does it, pass upon the question of the validity of a use tax under the assumed facts. The facts here show a principal use of the vessels in California fairly contemplated when the transaction occurred.

In *Southern Pacific v. Gallagher*, 306 U.S. 167; 83 L.Ed. 586, the railroad bought tangible personal property (rails, equipment, machinery, tools and office supplies) all outside of California. Some of the purchases were used in the general offices of the corporation in California, others were kept in readiness to make improvements and replacement. Storage was merely incidental to protection until use in both interstate and intrastate commerce. In the lower court, it was held that imposition of the use tax on these purchases violated the commerce clause.

The Supreme Court held, however, that the use and storage in California were taxable intrastate events. The Court says (on p. 177):

> "We think there was a taxable moment when the (articles) had reached the end of their interstate transportation and had not begun to be consumed in interstate operation. At that moment, the tax on storage and use—retention and exercise of a right of ownership respectively—was effective. The interstate movement was complete. The interstate consumption had not begun."

The principles of the *Gallagher* case seem applicable here. While the vessels were being used for rental purposes

in California, they were being used in an intrastate operation. In fact, principal use was in California an intrastate taxable use. While in California, the vessels derived the benefits afforded by its government. This, under the rule of Gallagher case, justifies the imposition of the use tax so that "all tangible personalty sold or utilized in California is taxed once for the support of the state government."

I conclude, therefore, that the tax here imposed does not violate the Commerce clause.

(5) *Does Imposition of the Use Tax Violate Constitutional Principles of Due Process (Jurisdiction to Tax)?*

Plaintiff takes the position that imposition by the State of California of the tax (admittedly the primary obligation of Cienega) upon plaintiff constitutes an implied admission that it "has no power over Cienega." It makes the further claim that to justify the imposition of any tax here there must be "some act which would manifest the jurisdictional presence of Cienega in this State." (Pltf's Opening Brief, p. 21). Plaintiff cites the case of *Miller v. Maryland*, 347 U.S. 340.

I think that plaintiff assumes too much in claiming that the imposition of the tax upon plaintiff is an implied admission of no power over Cienega. All that this legislative act implies to me is astuteness of the State in establishing a source and means of collection.

A study of the Supreme Court decision (by a court divided 6 to 3) in the *Miller* case does not convince me of its applicability here. There, a Delaware department store advertised for customers in Maryland, but conducted no mail order business. All goods sold to Maryland customers were bought at the store, although some were delivered across the state border into Maryland at the customers' request. The Maryland tax was attempted to be imposed

on the Delaware merchant. The majority opinion in holding the attempt to tax violated the due process clause distinguished the case from *General Trading Co. v. State Tax Commission*, 322 U.S. 335, where the out of state merchant had entered the taxing state through traveling salesmen conducting continuous solicitation. Although finding no taxable event under the facts there present, the court's opinion recognizes (on p. 345):

> "Also the keeping of tangible . . . personalty within a state may give it a similar taxable situs there . . . Certain activities or transaction carried on within a state *such as the use* and sale of property may give jurisdiction to tax whomsoever engages therein. . ."

Of course, if the claim of plaintiff that Cienega, in letting its vessels to plaintiff, was not making a use of them in California is correct, and if the court errs in finding that they were, then the *Miller* case would seem to be in point. But I must be consistent and, adhering to the position that Cienega as a lessor tangible personal property under a lease contemplating California utilization by the lessee, which in fact occurs, is itself both using and consuming its property in California, I must, and do, conclude (adopting the very reasoning of the *Miller* decision) that jurisdiction to tax Cienega exists.

The facts in the very recent case of *Scripto v. Carson* (March, 1960), 362 U.S. 207, were similar to those in the *General Trading Company* case excepting that solicitation was through general brokers. In holding the tax valid, the Supreme Court (per Clark, J. states):

> "There must be, as our Brother Jackson stated in *Miller Bros. Co. v. Maryland* . . . some definate link, some minimum connection between a state and the person, property or transaction it seeks to tax. We believe that such a nexus is present here. First, the

> tax is a nondiscriminatory exaction levied for the use and enjoyment of property which has been purchased by Florida residents and which has actually entered into and become a part of the mass of property in that State."

The court concluded that the case was controlled by the *General Trading Company* case.

SUMMARY

The reasoning stated above has convinced me, therefore:

(1) That the merchant whose business is to lease tangible personal property uses and consumes the property just as much as the customer who hires the property:

(2) That the provisions of the California Use Tax reach, and impose a tax upon, the purchaser of property purchased to be leased for use or consumption in California and which is used and consumed in California:

(3) That there was both a use in California and *a purchase for use* in California here within the terms of the statute:

(4) That the application of the tax to this transaction does not violate the commerce clause of the U.S. Constitution; and

(5) That it does not violate due process.

Defendant will prepare findings in accordance with this opinion.

Dated: March 17, 1961.

FRED R. PIERCE
Judge

Brobeck, Phleger & Harrison,
111 Sutter Street,
San Francisco, California.
Telephone: SUtter 1-0666.

Attorneys for Plaintiff.

In the Superior Court of the State of California in and for the County of Sacramento

No. 113643

Union Oil Company of California, a corporation,
Plaintiff,

vs.

State Board of Equalization of the State of California,
Defendant.

Filed April 3, 1961

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This cause came on regularly for trial on the 28th day of April, 1960, before the above-entitled Court sitting without a jury, the Honorable Fred R. Pierce, Judge Presiding, Brobeck, Phleger & Harrison, by John M. Naff, Jr., appearing for plaintiff, and Stanley Mosk, Attorney General of the State of California, by Ernest P. Goodman and John J. Klee, Jr., Deputy Attorneys General, appearing for defendant, a Stipulation of Facts signed by the respective parties was filed and received by the Court, and the cause having been thereafter submitted subsequent to the filing of

written briefs and the hearing of oral argument, the Court having considered the evidence and being fully advised in the premises, now makes its Findings of Fact and Conclusions of Law as follows:

Findings of Fact

I

The Court finds that the facts are as stated in the Stipulation of Facts and the Court hereby adopts said stipulation as its Findings of Fact in this matter.

II

The Court further finds that each and every allegation of the complaint herein, which is not included in the Stipulation of Facts or admitted by the answer, is untrue.

Conclusions of Law

From the foregoing Findings of Fact, the Court makes the following Conclusions of Law:

I.

The SS. Santa Paula and SS. Lompoc were purchased by Cienega from a retailer for use and consumption in the State of California and were used and consumed by Cienega in the State of California.

II.

That the assessment and collection of use tax by the State of California with respect to the use and consumption by Cienega of the SS. Santa Paula and SS. Lompoc in this State was duly and regularly made pursuant to the Sales and Use Tax Law.

III.

That there was an intrastate use and consumption of the SS. Santa Paula and SS. Lompoc in the State of California by Cienega to which the use tax validly applied.

IV.

That plaintiff take nothing by this action, that defendant have its costs of suit herein incurred in the sum of $ ....., and that judgment be entered accordingly.

Dated: April 3, 1961.

/s/ FRED R. PIERCE
Judge of the Superior Court.

Stanley Mosk, Attorney General
of the State of California
Ernest P. Goodman, Deputy Attorney General
John J. Klee, Jr., Deputy Attorney General
600 State Building
San Francisco 2, California
Tel: Underhill 1-8700
Attorneys for Defendant.

In the Superior Court of the State of California,
in and for the County of Sacramento

No. 113643

Union Oil Company of California,
a corporation,
Plaintiff,

vs.

State Board of Equalization of the State
of California,
Defendant.

Filed April 3, 1961

JUDGMENT

This cause came on regularly for trial on the 28th day of April, 1960, before the above-entitled court sitting without a jury, the Honorable Fred R. Pierce, Judge Presiding, Brobeck, Phleger & Harrison, by John M. Naff, Jr., appearing for plaintiff, and Stanley Mosk, Attorney General of the State of California, by Ernest P. Goodman and John J. Klee, Jr., Deputy Attorneys General, appearing for defendant, a Stipulation of Facts signed by the respective parties was filed and received by the court, and the cause having been thereafter submitted subsequent to the filing of written

briefs and the hearing of oral argument, the court having made and signed its Findings of Fact and Conclusions of Law herein and ordered that judgment be entered for defendant in accordance therewith,

NOW, THEREFORE, IT IS HEREBY ORDERED, ADJUDGED AND DECREED that plaintiff take nothing by its complaint and that defendant have judgment for its costs incurred herein in the sum of $.....

Dated: April 3, 1961.

/s/ FRED R. PIERCE
Judge of the Superior Court.

Appendix B

Cal. Stats. 1941, ch. 36, sec. 1, p. 533:

"6009. 'Use' includes the exercise of any right or power over tangible personal property incident to the ownership of that property, except that it does not include the sale of that property in the regular course of business."

Cal. Stats. 1941, ch. 36, sec. 1, p. 538:

"6201. An excise tax is hereby imposed on the storage, use, or other consumption in this State of tangible personal property purchased from a retailer on or after July 1, 1935, for storage, use, or other consumption in this State at the rate of 3 per cent of the sales price of the property.

6202. Every person storing, using, or otherwise consuming in this State tangible personal property purchased from a retailer is liable for the tax. His liability is not extinguished until the tax has been paid to this State except that a receipt from a retailer maintaining a place of business in this State or from a retailer who is authorized by the board, under such rules and regulations as it may prescribe, to collect the tax and who is, for the purposes of this part relating to the use tax, regarded as a retailer maintaining a place of business in this State, given to the purchaser pursuant to Section 6203, is sufficient to relieve the purchaser from further liability for the tax to which the receipt refers.

6203. Every retailer maintaining a place of business in this State and making sales of tangible personal property for storage, use, or other consumption in this State, not exempted under Chapter 4 of this part, shall, at the time of making the sales or, if the storage, use

or other consumption of the tangible personal property is not then taxable hereunder, at the time the storage, use, or other consumption becomes taxable, collect the tax from the purchaser and give to the purchaser a receipt therefor in the manner and form prescribed by the board."

Cal. Stats. 1948, ch. 12, sec. 4, p. 16:

"6201. An excise tax is hereby imposed on the storage, use, or other consumption in this State of tangible personal property purchased from any retailer on or after July 1, 1935, for storage, use, or other consumption in this State at the rate of 3 percent of the sales price of the property, and at the rate of 2½ percent on and after July 1, 1943, and to and including June 30, 1949, and at the rate of 3 percent thereafter."